

**BEFORE THE  
PUBLIC SERVICE COMMISSION OF WISCONSIN**

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Application of Wisconsin Public Service Corporation for  
Authority to Adjust Electric and Natural Gas Rates

Docket No. 6690-UR-117

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**INITIAL BRIEF OF THE CITIZENS UTILITY BOARD**

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The Citizens Utility Board (“CUB”) hereby submits its Initial Brief in the above-captioned matter. By order dated July 6, 2005, the Public Service Commission (“Commission or PSC”) approved CUB’s application for intervenor compensation to advocate concerning the prudence of the Spring 2005 outage at the KNPP plant, improving rate design and load management offerings for small-use customers, and on cost of service study (“COSS”) issues. *Application for Intervenor Compensation by the Citizens Utility Board*, Order, Docket No. 1-IC-358 (July 6, 2005). CUB addresses these and other issues below.

**I. INTRODUCTION.**

On April 1, 2005, Wisconsin Public Service Corporation (“WPSC” or “the Company”) filed its application to change its rates effective January 1, 2006. (Tr. 121.) It requested an \$89.7 million (11.4%) increase for electric operations and a \$10.0 million (2.1%) increase for natural gas operations. (Tr. 122.) After adjustments to WPSC’s application, Staff’s audit estimated increases of \$52.7 million (6.7%) and \$7.3 million (5.7%) for the Company’s electric and gas operations respectively. (*Id.*)

Shortly before hearing, WPSC stated that recent hurricanes had caused sharp rises in natural gas prices, resulting in an increase in WPSC’s projected natural gas costs for electric generation of \$58.9 million above staff-audited levels. (Tr. 590-91.) Suddenly, a 6.7% increase became a 14.2% increase.

WPSC's rate application therefore poses a substantial challenge for this Commission to mitigate the impacts of dramatically higher costs for fuel used in electric generation. To meet this challenge and help avoid rate shock, the Commission should reject as unfair to ratepayers WPSC's so-called Wind-Up Plan relating to the sale of the Kewaunee Nuclear Power Plant ("KNPP"), including the Company's proposed slow-motion return of the NonQualified Decommissioning Trust Fund ("NQF"). In conjunction with its Wind-Up Plan review, the Commission should also reject rate recovery for WPSC's deferred replacement power costs associated with the KNPP 2005 spring outage on the grounds of imprudency and as contrary to the fuel rules. CUB also urges the Commission as part of this proceeding to revisit long-standing policies and regulatory assumptions concerning the state's electric industry, particularly the appropriate return on equity and capital structure. Additionally, the Commission should insist on rapid implementation of innovative rate designs to complement small customer load management initiatives. Finally, at a time of significant rate pressures, it is especially imperative that the Commission be guided by proper cost of service studies that reflect cost allocations based on causation. To do otherwise is to inflict unjust and harsh results on customers.

## **II. THE COMMISSION SHOULD REJECT WPSC'S KNPP WIND-UP PLAN.**

WPSC asks the Commission to approve its so-called Wind-Up Plan in which the Company, as a result of its sale of the KNPP, proposes to return over a five-year period \$127 million of NQF monies to its ratepayers minus the amounts for several items, including the Company's loss on the sale of the plant and its outstanding deferrals associated with the plant's 2004 and 2005 outages. (Tr. 292-95.) WPSC made this proposal jointly to the Commission as part of this rate proceeding and to the Federal Energy Regulatory Commission ("FERC"). (Tr. 289.)

CUB requests that the Commission reject WPSC's so-called Wind-Up Plan because it proposes to: 1) return NQF monies over five years rather than two years as supported by CUB; 2) **\*\*\*BEGIN CONFIDENTIAL\*\*\***

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**CONFIDENTIAL\*\*\*** 4) require rate recovery for WPSC's replacement power costs associated with the KNPP 2005 spring outage.

As noted above, WPSC has also filed its so-called "Wind Up Plan" with FERC. FERC accepted the plan for filing, but to its credit suspended the plan and set it to hearing, noting that "[o]ur preliminary analysis indicates that WPSC's proposal has not been shown to be just and reasonable, and may be unjust, unreasonable, unduly discriminatory or preferential, or otherwise unlawful." *Order Accepting And Suspending Proposed Refund Plan, Instituting Investigation, Establishing Refund Effective Date and Hearing and Settlement Judge Procedures, and Consolidating Dockets*, Docket Nos. ER05-1089-000, AC05-54-000, EL05-136-000, 112 FERC ¶ 61,165 at par. 21 (August 4, 2005). FERC has yet to take final action on the proposal.

**A. Consistent With Its Decision In The WPL Rate Case, The Commission Should Require WPSC To Return The NQF Over A Two-Year Period.**

WPSC proposes to amortize return of the NQF over a five-year period. (Tr. 292-93.) A major justification for its choosing a five-year period is its concern with rate shock. (Tr. 292, 334-38.) PSC Staff witness Thomas Ferris identified both eight and three years as possible periods for the Commission to consider for return of the NQF monies. (Tr. 133, 146-47.) CUB submits that the Commission should reject WPSC's and Staff's identified options as failing to take into account the impact of presently high fuel costs, as inequitable for a variety of reasons,

and as inconsistent with the Commission's decision for a two-year return of the NQF monies in the 2005-06 WPL rate case.

WPSC supports the amortization of the NQF over five years as a way to avoid rate shock in future years. (Tr. 334-38.) Ironically, the Company fails to take into account the rate shock that ratepayers will feel here and now due to the hurricane-caused rising costs of natural gas. WPSC itself testified that rising costs attributable to natural gas would push up rates \$58.9 million beyond staff-audited levels. (Tr. 591.) Offsetting this price spike with NQF monies would seem especially appropriate to avoid the harsh results which otherwise might occur to all classes of ratepayers, residential and business alike.

For the same reason, the Commission should reject Staff's proposed eight- and three-year alternatives for the return of the NQF monies. Staff suggested that an eight-year return of the NQF may be appropriate since it would be tied to the length of WPSC's Purchase Power Agreement ("PPA") with DEK. (Tr. 133.) But there is no logical link between return of the NQF and the duration of the KNPP PPA other than to say that both obviously involve the KNPP. Adoption of Staff's proposed three-year return of NQF monies to coincide with WPSC's biennial rate schedule would amount to placing greater emphasis on the workings of regulation over the critical need of ratepayers for help in the face of higher energy prices. Besides, WPSC is a regular supplicant to the Commission, and it seems doubtful that the Company would forego an annual rate case notwithstanding any biennial rate case schedule.

Furthermore, delayed return of the NQF monies is inequitable. WPSC collected the NQF monies for a single utility purpose—decommissioning the KNPP. (Tr. 894.) Those funds were never intended to be used for any other purpose, including as an offset to other utility expenses. Moreover, a faster return of the monies best serves intergenerational equity by helping to ensure

that the funds are received by the ratepayers who actually paid them. (*Id.*) Finally, there is no linkage that requires the amortization of the return of the NQF monies to be the same as recovery of WPSC's deferred costs since the justifications for each are different.

The Wisconsin Industrial Energy Group and representatives of the paper industry agree with CUB. (Tr. 97, 106-09, 424-25.) Testifying for Wausau Paper Corporation, Mr. Steven Smith noted that the amount of the NQF due customers was "not the consequence of a voluntary loan to WPS from its consumers. Customers should therefore not be obligated to leave their money with WPS." (Tr. 106.) Additionally, business customers of WPS may have a higher cost of capital than WPS, and delays in returning the NQF cost these customers money. (*Id.*)

This Commission correctly decided to return the NQF monies over a two-year period in the WPL rate case, and no party in this proceeding has explained why it would be fair to WPSC ratepayers to be treated differently than WPL ratepayers if a longer amortization period is adopted. (Tr. 895, citing Final Decision, Docket No. 6680-UR-114, Finding of Fact 26 at 6.) Consistent with its decision in the WPL rate case, the Commission should require return of the NQF monies over a two-year period.

**B. Shareholders, Not Ratepayers, Should Pay For WPSC's Loss On The Sale Of The KNPP.**

WPSC's adjusted proceeds on the sale of the KNPP were \$115.2 million. (Tr. 310.) The estimated book value of the transferred assets was \$110 million, yielding a net gain to WPSC of \$4.2 million. (*Id.*) WPSC proposes to net against this amount several items including losses it incurred as a result of risks it took in order to close the sale of KNPP. One of these losses was the recorded loss on contingent purchase price adjustments due DEK under a settlement agreement as a result of the Spring 2005 outage. That loss is included in the total recorded loss on the sale of the plant of \$12.5 million that WPSC proposes to net against the gain. (Tr. 310;

314.) In addition, **\*\*\*BEGIN CONFIDENTIAL\*\*\***

**\*\*\*END CONFIDENTIAL\*\*\*** CUB submits that WPSC's shareholders, not ratepayers, should bear the burden of these losses because they result from management imprudence.

1. **WPSC proposes that ratepayers bear the burden of the risks it took selling the plant.**

Before the sale, **\*\*\*BEGIN CONFIDENTIAL\*\*\***

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arising from the Spring 2005 outage. (Tr. 1282-83.) WPSC took these actions as a result of bargaining by DEK subsequent to this Commission's approval of the sale of KNPP.

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**2. The adjustments made to the transaction at DEK's insistence arise from NMC's imprudence.**

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These costs would not have arisen had NMC been properly running the plant. Ratepayers should not be required to subsidize imprudent utility management. Therefore, WPSC's shareholder should bear these costs.

**C. The Commission Should Disallow Rate Recovery For WPSC's Purchased Power Costs Associated With The Spring 2005 Outage Due To The Company's Imprudence And As Contrary To The Fuel Rules.**

Throughout the Spring 2005 outage of KNPP, WPSC incurred replacement energy costs. WPSC requests rate recovery from the Commission for these purchased power costs in the amount of \$41,223,772. (Tr. 1167.) The Commission should reject WPSC's request because the

outage was due to NMC's<sup>1</sup> and WPSC's imprudent management of KNPP. Moreover, WPSC's request should be denied because it is not in compliance with section 116.03(5) of the fuel rules.

**1. Management's imprudence caused the Spring 2005 outage.**

Prudence is a factor the Commission can consider when setting utility rates, and the Commission has wide discretion in dealing with the issue of imprudence. *See Wisconsin Pub. Serv. Corp. v. Pub. Serv. Comm'n*, 156 Wis. 2d 611, 616 (Ct. App. 1990). The party asserting that a utility has acted imprudently has the burden of proof on that issue. *See Waukesha Gas & Electric Co. v. Railroad Commission*, 181 Wis. 281, 304 (1923) ("In the absence of satisfactory proof to the contrary it must be presumed that the investment was prudently made.") The standard of prudence is essentially a "reasonable man standard" in that utilities' actions or decisions are compared to the reasonable actions or decisions of a qualified and experienced utility manager given what was known, or what should have been known, at the time without benefit of hindsight. (Tr. 1303.) The Wisconsin Court of Appeals has defined prudence as:

Carefulness, precaution, attentiveness and good judgment, as applied to action or conduct . . . . This term, in the language of the law, is commonly associated with "care" and "diligence" and contrasted with "negligence."

(*Id.*, citing *Wisconsin Pub. Serv. Corp.*, at 617.) This Commission has further elaborated, "Imprudence, according to the court, is the waste of assets, the lack of caution, the failure to take reasonable steps to protect assets." (*Id.*, citing Amended Findings of Fact, Amended Conclusions of Law and Conditional Order, Docket No. 6630-UR-109 (December 23, 1997).) Ratepayers should not be required to pay for costs associated with a utility's imprudent management decisions.

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<sup>1</sup> Because NMC was, at all times, acting on behalf of and at the request of WPSC, WPSC is responsible for the consequences of NMC's actions. Therefore, any reference to NMC necessarily implicates WPSC.



**a. The Company had many opportunities to identify and correct the deficiencies with the auxiliary feed water system prior to the Spring 2005.**

The Company claims that the “sole cause” of the outage was NMC’s finding of inoperability with respect to the auxiliary feed water (“AFW”) system, and that the only reason this finding was made was because NRC identified a “new” and “more conservative” failure mode for the AFW pumps in 2005. (Tr. 1172.) However, the potential for air ingestion and subsequent pump damage that NRC identified was neither new nor more conservative. (Tr. 1339.) A review of the history of concerns with the AFW system design shows that the problems existed since the AFW system was put in place, and that the Company had numerous opportunities to correct the problems prior to the spring of 2005.

The AFW system at KNPP was originally designed in the late 1960s and early 1970s. (Tr. 1173.) Proper functioning of the AFW system is necessary to cool down the plant if certain events occur (i.e. tornados, earthquakes, etc.). (Tr. 1307.) Inoperable AFW pumps can lead to a serious accident, including core melting under some conditions. (*Id.*) In 1979, following the Three Mile Island event, the NRC issued a regulation requiring nuclear plant owners to take additional steps to ensure that AFW pumps would remain operable during postulated seismic and tornado events. (*Id.*) Also in 1979, the NRC sent a letter to WPSC advising the Company of additional requirements for KNPP’s AFW system in light of the Three Mile Island accident. (Exh. 91, at 8.) Over the next several years, WPSC and NRC exchanged numerous letters regarding these requirements. (Exh. 91, at 9.) In 1983, WPSC sent another letter to the NRC proposing the installation of automatic trips to protect the AFW pumps on loss of suction. The NRC accepted this proposal and DCR 1371 was initiated in May 1983 to install the automatic AFW pump suction trips. (*Id.*)

Nearly 10 years later, WPSC still had not installed the automatic suction pressure trips they had committed to install in May 1983. (Exh. 91, at 10.) In February 1993, WPSC sent a letter to the NRC apologizing for the delay. (*Id.*) The Company finally moved forward on its plan to install the low suction pressure trips on February 2, 1993. In May 1993, WPSC sent another letter to NRC proposing to change the suction pressure trips to discharge pressure trips. (*Id.*) NRC sent WPSC a letter on June 8, 1993, granting WPSC's request to change to discharge pressure trips. (Tr. 1341-42.)

In 1997, an NRC inspection team questioned the discharge pressure switch setpoint for the turbine driven AFW pump. (Exh. 91, at 11.) The NRC inspection report also noted, "Overall, the results of the System Operational Performance Inspection (SOPI) raised concerns about the rigor of engineering efforts in general, and, in particular, with maintaining the design basis performance of safety-related pumps through an effective surveillance program." (Tr. 1331.) In response, the Company reviewed the discharge pressure switch setpoint issue and determined that the basis for the setpoint was not clear. The Company made some minor modifications to a calculation, but did nothing more. (Exh. 91, at 11.)

At the end of 2004, NRC informed WPSC that KNPP would be one of four nuclear plants for which NRC would conduct a "High Risk/Low Margin" inspection.<sup>2</sup> (Tr. 1306.) The inspection was scheduled to begin in January 2005. (Tr. 1163.) KNPP was the last of the four plants inspected, and KNPP staff discussed the other inspections with the staffs of the other plants prior to the KNPP inspection. (Tr. 1306.)

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<sup>2</sup> As the name implies, this type of inspection focuses on aspects of a plant's design that represent a relatively high degree of risk and for which there appears to be a relatively low margin. (Tr. 1305.) In this context, "low margin" means in an accident condition, the component or system must operate at or near its full capacity with little room for operator error or equipment malfunction. (Tr. 1305-06.)

Prior to the inspection, the NRC gave notice to WPSC that the plant's AFW system would be a part of the review. (Tr. 1205.) On January 24, 2005, in preparation for the inspection, NMC identified the lack of a definitive basis for the AFW pump discharge pressure trip setpoints as a concern. (Tr. 1307.) Three days later, NRC asked NMC if the potential for air ingestion had been considered when the discharge pressure trip setpoints were established. (*Id.*) This question led to an evaluation of the AFW system to determine whether it would function properly in the event of a tornado or earthquake. On February 4, 2005, NMC concluded that the AFW system was operable, but that NMC could not demonstrate that the AFW pumps would be protected if certain events occurred. (Tr. 1307-08.)

Three days later, on February 7, 2005, NMC approved Operability Recommendation OPR-087 concluding that the AFW system was "operable but degraded." (Tr. 1308.) The NRC questioned this conclusion because NMC's operability recommendation still did not take into account possible seismic or tornadic events. (*Id.*) On February 8, 2005, NMC approved a revision to the operability recommendation adding a dedicated control room operator and procedure changes regarding the AFW pumps in the event of an earthquake or tornado, but the revision continued to state that no compensatory measures to the AFW system were needed. (*Id.*) The next day, NMC issued a second revision to the recommendation providing that even if suction to the AFW pumps was lost, there was a reasonable assurance that the pumps would not be damaged before the discharge pressure trips stopped the pumps. (*Id.*)

Two days later, NMC reversed its position and declared the discharge pressure trips on all of KNPP's AFW pumps to be inoperable based on the potential for damage during a tornado. NMC then initiated compensatory measures. (Tr. 1309.) However, NMC did not issue a revision to the operability recommendation. The next day, NMC again reversed its position

declaring the discharge pressure trips to be operable but non-conforming. (*Id.*) One day later, on February 13, 2005, NMC issued a third revision to the operability recommendation, this time addressing the compensatory measures, but still declaring the AFW pumps operable. (*Id.*) NRC continued to question the technical bases for NMC's conclusions. Finally, on February 19, 2005, the day after NRC completed its on-site inspection, NMC determined that the AFW pump suction piping system was susceptible to damage from a high energy line break, and it declared all of KNPP's AFW pumps inoperable and began shutting down the plant. (Tr. 1165; 1309.)

Shortly after KNPP was shut down, NMC submitted a 19-page commitment list to NRC identifying specific objectives and actions to be completed in the following areas:

- Operations Leadership;
- Configuration Management;
- Engineering Effectiveness;
- Corrective Action Program Effectiveness; and
- Manager/Supervisor Effectiveness.

(Tr. 1311.) Many of the items on the commitment list were required to be resolved prior to restarting the unit. (Tr. 1312.) In addition, some of the specific issues, such as the fact that the Emergency Diesel Generator Exhaust was not adequately protected from potential tornado winds and missiles and that the turbine building was susceptible to flooding would likely have required plant shutdown independently of the AFW pump issues. (Tr. 1322-23.)

On March 22, 2005, after the commitment list had been issued, the NRC Executive Director of Operations visited the KNPP site. (Tr. 1253.) He told NMC officials that they needed to identify all issues that needed to be resolved before startup and have "frequent, quality communications with NRC." (*Id.*) One week later, in a meeting between WPSC, NMC, DEK,

and NRC, the NRC executive director reported that he was “troubled” by what he saw during his visit to KNPP, and he was particularly concerned with the apparent lack of a consolidated plan by NMC for the restart of the unit. (*Id.*) The WPSC nuclear management team also followed the outage issues closely and had similar observations to those of NRC. (*Id.*) NMC was having difficulty finding qualified engineering support to investigate and resolve the issues. (Tr. 1254.)

There was also a concern about the number of key plant positions that were vacant or being filled by temporary employees “as a result of the extraordinarily long transition period” for the sale.<sup>3</sup> (*Id.*) The problem was so grave that NMC had to enter into a separate contract with DEK in order to fill the vacant positions. (*Id.*) Meanwhile, the number of problems that needed to be resolved prior to restarting the plant continued to grow. The outage began on February 20, 2005 and WPSC initially projected that KNPP would be back on line in late March or early April 2005. (Exh. 76.) In fact, there were numerous projected startup dates: late March 2005, April 8, 2005, April 14, 2005, April 22, 2005, early May 2005, May 22, 2005, early June 2005, and late June 2005. (*Id.*)

Charles Schrock (WPSC’s President and Chief Operating Officer for Generation) testified as to the delay, “As NMC was working through the extent of condition reviews, new items that had to be corrected were being discovered, making it difficult to definitively identify the scope and schedule for the outage.” (Tr. 1251; 1253.) WPSC also noted that, “[t]he extent of condition review [including items from the March 18 commitment list] and the issues that were being identified and resolved in that review caused the dates to slip in the month of April.” (Exh. 76; Tr. 1212-13.) In addition, WPSC testified, “The completion of the extent of condition review and the resolution of issues identified during this review took longer than initially

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<sup>3</sup> The following key positions, among others, were vacant at the time: Site Vice President, Operations Manager, Design Engineering Manager, Oversight Manager, and Training Manager. (Tr. 1254.)

expected.” (Tr. 1166.) In fact, in response to another data request from CUB asking for a description of *each issue that delayed completion of the outage*, WPSC provided a comprehensive list of items that delayed completion including many issues from the March 18<sup>th</sup> commitment letter. (Tr. 1346-53.)

Moreover, toward the end of April, the plant staff also determined that the NRC needed to approve a Technical Specification license amendment for the AFW system issues prior to startup. (Exh. 76.) The NMC had scheduled to send the amendment in late April, but did not file it until early May. (*Id.*) NMC then identified additional issues regarding the residual heat removal (“RHR”) pumps and submitted a second Technical Specification license amendment to NRC in late May. (*Id.*) WPSC received the NRC license amendment for the AFW modifications in mid-June 2005 and the license amendment for the RHR pump concerns in late June. (Tr. 1216.) The unit did not come back onto the grid until July 2, 2005. (Exh. 76.)

**b. As the root cause evaluation demonstrates, the Company’s imprudence was the cause of the Spring 2005 outage.**

Following the outage of KNPP, NMC issued a root cause evaluation addressing the AFW system issues. A root cause evaluation probes the history and events leading up to an outage and identifies deficiencies that were or should have been known and corrected prior to the outage. (Tr. 1364-65.) Although a root cause evaluation is, by necessity, retrospective, use of a root cause analysis to identify the cause of an event and what could have been done to prevent the event is not 20/20 hindsight. (Tr. 1365.)

The reasons identified in the Root Cause Analysis explain why WPSC did not correct the AFW system deficiencies:

Root Cause:

RC#1 - Engineering had a lack of knowledge and understanding of what constituted a proper rigor of analysis, review, or documentation when resolving issues related to design basis for the AFW pumps.

(Tr. 1324.)

A full understanding and appreciation of this root cause is key to understanding the cause of the outage. In 1993, when WPSC modified the design of the discharge pressure trips, WPSC did not have the knowledge and understanding of the type and depth of analysis needed to ensure a fully functional design in order to correct the AFW system deficiencies. WPSC did not know and understand the level of review needed for this design, and it did not know or understand the documentation that was required to support this design. An engineering department that makes modifications to a critical safety system without an understanding of the required analysis, review, and documentation of the design is imprudent. This is the fundamental cause of the Spring 2005 outage. (Tr. 1317.)

In its root cause evaluation, NMC also identified the following support for the root cause shown above:

- Lack of detail in design basis for DCR 2668 for switching from suction trips to discharge pressure trips.
- Modification that was installed to protect the AFW pumps was only focused on one aspect of failure mechanism and did not take into account all effects from that failure mechanism.
- Mindset that discharge pressure switches and transport time were adequate to protect the pump influenced the site's failure to recognize OE [Operating Experience] related air entrainment issues with respect to the AFW pumps.
- Lack of documented analysis and basis for setpoints of discharge pressure trips.
- Inadequate use of vendor documentation for an unrelated but similar issue without documented follow-up with the vendor to ensure applicability.

- There was an inadequate understanding of the work that needed to be performed and the significance of not performing the modification related to installation of the suction pressure trips and as such the modification was delayed almost 10 years before it was realized that a commitment was not satisfied and the AFW pumps were not protected.
- Failure to ensure that the modification for the low suction pressure switches contained adequate documentation on the basis for changing the scope of the modification and the basis for the setpoints for the discharge pressure switches even after the 1997 SOPI where the NRC questioned these setpoint bases.

(Tr. 1325.) In addition, NMC identified the following contributing causes to the Company's failure to correct the AFW system deficiencies in 1993:

SC#1 – There was a lack of commitment at the site to adequately develop and install the modification to provide automatic protection to the AFW pumps from a loss of suction.

- Long-standing resistance to installing modification for low suction pressure switches over a 10-year period.
- Clear language in letter that committed to installing the AFW suction pressure trips that indicated the site still believed there would only be a minimal increase in benefit.
- Minimalist approach to implementation of AFW protection scheme.
- Inadequate use of vendor documentation for an unrelated but similar issue without documented follow-up with the vendor to ensure applicability.

SC#2 – Weak program and process guidance and expectations over time have hindered the site in fulfilling obligations.

- The commitment-tracking program was an inadequate tracking mechanism to ensure that the commitment made to the NRC was fulfilled.
- Due dates were not given/enforced and communication with the NRC was lacking in relation to low suction pressure trip modification in the 1980s and 1990s.
- The standards and expectations used 12 years ago were weaker than current standards and expectations and it is generally recognized that the site has historically had a strong "knowledge of the craft" culture in the past.
- The site was a stand-alone plant relying on internalized inputs and resolutions more than external inputs and guidance for issue resolution.



SC#3 – Poor planning and issue management resulted in issues not being properly addressed in a timely manner and involved numerous items of rework based on promptings by the NRC.

- Repeat prompting by the NRC for updates related to GL-4 went effectively unanswered for several correspondences.
- The site did not install the modification in a timely manner, referring to evaluations being performed for PRA and IPE as justification for delays and proof that only a marginal increase in safety would be obtained by installing the modification.
- It took four years to perform evaluation for GL-4 that the site said would be evaluated in 90 days.

(Tr. 1325-26.)

In the narrative sections of the root cause evaluation, NMC also noted that the problems were long-standing since the early 1980s:

Overall, insufficient detail and documentation for the original Kewaunee design basis and continued lack of detail and documentation for subsequent work performed related to the AFW design basis, resulted in a persistent flawed analytical model of the system design basis and a lack of understanding of the intended modification scope that was needed to protect the AFW pumps. This mindset has persisted from the early 1980s until the present day when the issue with the discharge pressure switches was discovered during review of the system in preparation for the NRC HRLM [High Risk/Low Margin] inspection.

(Exh. 91, at 31.)

From the 1980s to the 1990s, there was a lack in rigor needed to document and review actions taken related to the commitment made to the NRC to install AFW low suction pressure trips and to follow-up with the NRC after the choice was made to not pursue that option. There was a lack of rigor in the analysis, review and level of documentation needed to adequately justify changing the scope of DCR 2668 from the suction pressure trips to the discharge pressure trips in 1993.

There was a lack of rigor of analysis, review and quality of documentation for OPR 087 that resulted in three official revisions and a fourth unofficial revision, that was required to ensure that the plant made a conservative call on whether the pumps should have been called operable but non-conforming or inoperable, both by the personnel involved with providing the analysis (Engineering) and the personnel required to act on that analysis (Operations).

(Exh. 91, at 35.)

Moreover, NMC determined that the root causes for one of the issues from the commitment list, the turbine building flooding, were similar to the root cause for the AFW pump issue, namely:

RC1 - When told we have problems, the site does not recognize the possible significance of the problem and apply the appropriate actions commensurate with the significance of the problems to fix them.

RC2 - KNPP personnel have developed a minimalist approach to making changes.

(Tr. 1327.)

In addition, in an inspection report following the restart of the plant in July 2005, NRC noted that:

The inspectors determined that a performance deficiency exists; the issue associated with potential air ingestion was NRC-identified; and the issue associated with potential runout protection resulted from inspector questions surrounding the discharge switches that *should have been identified in previous pump performance evaluations in 1997*.

(Exh. 92, at 11, *emphasis added*.)

The root cause evaluation and NRC's report demonstrate that the problem with the AFW pumps was a long-standing issue that management neglected to previously identify or adequately address. (Tr. 1329.) WPSC could have addressed this issue in the early 1980's after WPSC made the commitment to NRC to install low suction pressure trips. (Exh. 91, at 35.) WPSC could have resolved the problem in 1993 when it modified the discharge pressure trips. (*Id.*) As NRC also noted, WPSC should have addressed this issue in 1997 during the pump performance evaluations. (Exh. 92, at 11.)

Instead, critical design flaws in KNPP's AFW system were not discovered by WPSC for over 30 years, but were discovered after only three days of questioning from NRC. (Tr. 1339.)

WPSC was negligent given what was known or should have been known from the time the AFW system was constructed until NRC prompted the discovery of the problem. The root cause evaluation demonstrates that WPSC acted imprudently. Therefore, all purchase power costs associated with the outage should be disallowed.

**c. The Commission should not allow WPSC to shift the blame for the outage to NRC.**

WPSC denies that it acted imprudently, and it attempts to shift the blame for the outage to the NRC. WPSC blames NRC by asserting that the “sole cause” of the Spring 2005 outage was NMC’s finding of inoperability with respect to the AFW system, and the only reason this finding was made was because NRC issued a “new” and “more conservative” failure mode for the AFW pumps. (Tr. 1172.) WPSC is wrong, and WPSC’s attempt to shift blame for its mismanagement should be rejected.

WPSC argues that, if NRC had not raised its standards by issuing a “new” and “more conservative” failure mode for the AFW pumps, there would have been no outage because NMC’s finding based on NRC’s standards was the “sole cause” for the outage. (Tr. 1172.) First, NRC did not identify a “new” or “more conservative” failure mode. (Tr. 1339.) The potential for loss of suction and air ingestion identified by NRC is a significant concern for a safety-related pump that a prudent owner would consider without prompting from NRC. (*Id.*) As stated above, the root cause evaluation noted WPSC’s failure to recognize relevant operating experience as a contributing cause in this event. However, WPSC appears to think it is NRC’s duty to identify potential issues for pump damage and not the duty of the plant owners and operators. (*Id.*) But the duty and responsibility for the safe design, maintenance and operation of a nuclear power plant *always* remains with the plant owner. (Tr. 1340.) A nuclear plant owner can never shift responsibility or blame for its deficiencies to the NRC. (*Id.*)

Nor can a nuclear plant owner assert, as WPSC tried to do, that it is NRC's fault because it "approved" a prior modification in the design of the AFW plant without noting any issues with respect to the potential for inoperability of the pumps. (Tr. 1173; 1340.) As a practical matter, the NRC cannot conduct a detailed engineering review of every design change submitted to them for review. (Tr. 1341.) Instead, it relies on plant owners to be competent and to produce design changes that meet all required regulations and maintain the design basis of the plant. (*Id.*) In fact, the NRC did not even "approve" WPSC's design change. In its letter on June 8, 1993 concerning the AFW pump modifications, the NRC stated, "The staff has reviewed these changes [moving the AFW pump trips from the suction to the discharge side of the pumps] in your commitments and finds them acceptable." Thus, the NRC merely reviewed the changes as represented and did not approve the system's design. (Tr. 1341-42.)

Moreover, although the AFW problems were the initiating event for the outage, they were not the "sole cause" as stated by WPSC. (Tr. 1338.) As discussed above, almost as soon as KNPP was shut down, NMC began putting together a list of additional concerns and issues symptomatic of much broader management and programmatic weaknesses throughout KNPP that needed to be resolved prior to restarting the unit. (Tr. 1311-12.) The AFW pump issues and the issues on the commitment list were long-standing issues that had been previously identified and not adequately addressed. (Tr. 1329.) Reasonable and prudent management would have taken timely and effective corrective action to prevent development of the conditions that led to the need for the correction of the extensive programmatic and management failures that caused the outage to extend for months beyond original projections. (Tr. 1334.) NRC is not to blame for the outage; WPSC is. Therefore, WPSC's ratepayers should not pay for the costs associated with the length of the outage.

**2. WPSC’s request for rate recovery for the purchased power costs associated with the Spring 2005 outage is contrary to the fuel rules.**

WPSC is requesting rate recovery for the purchased power costs associated with the Spring 2005 outage pursuant to Wis. Admin. Code § PSC 116.06 (Emergencies) of the fuel rules. A utility requesting rate recovery under the fuel rules bears the burden of proving the elements necessary to justify deferral of the fuel expenses. *See e.g. Sterlingworth Condominium Assoc. v. Dept. of Natural Resources*, 205 Wis. 2d 710, 726 (Ct. App. 1996) (“The customary common-law rule that the moving party has the burden of proof, including not only the burden of going forward but also the burden of persuasion, is generally observed in administrative hearings.”). As Staff witness Randy Hillebrand explained, in order for WPSC to demonstrate that it is entitled to rate recovery for the purchased power costs, it must prove that it experienced an “emergency.” (Tr. 742.) The code defines an “emergency” as an event that:

- (a) Is caused *suddenly* by forces beyond the utility’s control or reasonable foresight; *and*
- (b) Causes expenditures that are unusual and infrequently recurring; *and*
- (c) Causes the utility to incur added costs appropriate for recognition in . . . an amount at least as great as the amount of fuel costs necessary to show an extraordinary increase in the cost of fuel.

Wis. Admin. Code § PSC 116.03(5) (*emphasis added*). Its clear from the language of the code that all three conditions must be met before an emergency occurs.

As discussed in detail in section 1 above, many of the problems that led to the outage at KNPP were long-standing and the result of NMC taking a minimalist approach to engineering as well as the failure of the management and the corrective action program to recognize the significance of issues and take timely and effective corrective action. (Tr. 1334-35.) WPSC has not met its burden in proving that the Spring 2005 outage was caused suddenly by forces beyond

its control or reasonable foresight. As the root cause evaluation and NRC's report indicate, NMC, and WPSC before it, WPSC could, and should, have foreseen the problems with the AFW system long before NRC brought the issue to its attention in the early part of 2005. There was nothing "sudden" about the cause of this outage. The causes of the problems were clearly within WPSC's ability to control and foresee. (Tr. 1335; Exh. 92, at 11.) Therefore, the KNPP outage does not meet the first prong of the test for defining an "emergency" event, and WPSC should not be allowed to recover from ratepayers its costs for the replacement fuel during the outage.

**D. The NonQualified Fund Was Not Created To Wash Away Management's Mistakes.**

The NQF exists for one purpose and one purpose only, i.e. to decommission the KNPP. (Tr. 894.) **\*\*\*BEGIN CONFIDENTIAL\*\*\***

**\*\*\*END CONFIDENTIAL\*\*\*** As the Commission determined when it approved the sale of KNPP, the funds are to be returned to those who paid them, i.e. ratepayers. As discussed in the sections above, the Commission should: (1) authorize return of the NQF to ratepayers over a two-year period; (2) require shareholders, not ratepayers, to shoulder the losses occasioned by the sale of KNPP; and (3) disallow rate recovery for the replacement fuel costs associated with the Company's imprudence in managing the plant prior to the Spring 2005 outage.

**III. THE COMMISSION SHOULD TAKE STEPS TO MITIGATE THE RISING COSTS OF NATURAL GAS RATES AND COAL PRICES.**

To mitigate rate hikes due to the higher fuel costs for electric generation, this Commission should recognize that not just ratepayers but also the utility and its shareholders must bear some of the costs that would otherwise push rates higher.

To its credit, WPSC decided to forego some \$20 million in rate recovery for certain O&M expenditures with its rate filing. (Tr. 130.) But this Commission cannot stop there, and must do all it can to adopt regulatory policies that mitigate rate hikes while still providing a fair and reasonable return to shareholders under reasonable capital structures. To this end, CUB urges the Commission to adopt a return on equity for WPSC at 10%, or in the alternative, no higher than 10.5% and to oppose the Company's plan for a higher than necessary equity to debt ratio as part of its capital structure.

**A. The Consequences Of Higher Fuel Costs Should Be Borne Not Just By Ratepayers, But Also Shareholders.**

For this proceeding, WPSC assumed an 11.5% return on common equity for its rate case, consistent with its prior rate order. (Tr. 15.) Based on its analysis, Commission Staff suggested that a reasonable range of equity for WPSC in the test year is 10% to 11.5% with 11% used as a point estimate. (Tr. 473.) Commission Staff proposed 11% in part to implement a “principal [sic] of gradualism, moving the authorized return closer to the required return.” (*Id.*) Adopting Commission Staff's gradualist approach saves ratepayers roughly \$6.9 million in the test year. (Exh. 14, Schedules 9 and 10, Tr. 162-64.)

The Wisconsin Industrial Energy Group proposed a 10.5% ROE. WIEG testified that a 10.5% ROE would support WPSC's A+ S&P credit rating. (Tr. 386.) Addressing the economic impact of ROE determinations, Mr. Gorman stated that failing to take advantage of low cost capital market cost pricing in utility services “will negatively impact the state of Wisconsin's ability to retain and attract businesses that compete outside of Wisconsin for jobs and investment capital.” (*Id.*) To adopt WIEG's proposed ROE saves ratepayers nearly \$13.7 million compared to maintaining an 11.5% ROE for WPSC. (Exh. 14, Schedules 9 and 10, Tr. 162-64.)

At a time of dramatically rising rates, it is unthinkable that WPSC shareholders should not have to bear some burden. Wausau Paper Company witness Steven Smith testified concerning the effects of the last rate case to highlight this point:

Group	Dollar Impact (in millions)	% Impact
Commercial and Industrial	\$31.8 million	9.74%
Residential	\$28.9 million	7.56%
<i><b>WPS Stockholders</b></i>	<i><b>\$0</b></i>	<i><b>0.00%</b></i>
Total Economic Impact	\$60.7 million	8.57%

(Tr. 104.) (Emphasis added.) To help offset the \$58 million increase in fuel costs projected by WPSC above staff-audited levels, CUB favors lowering ROE levels to 10%, a move that would save ratepayers \$20.5 million compared to an ROE of 11.5% as sought by the Company. (Exh. 14, Schedules 9 and 10, Tr. 162-64.) In the alternative, the Commission should adopt WIEG's position and establish ROE no higher than 10.5%.

**B. The Commission Should Reject WPSC's Request For A Financial Basis Common Equity Range Of 54% to 58%.**

In its last rate decision involving WPSC, the Commission approved a long-term range of 54% to 58% common equity on a financial basis. (Tr. 457.) Despite this action, Standard and Poors lowered WPSC's corporate rating to "A+" from "AA-" only five weeks after the Commission's decision. (Tr. 457; Final Decision, Docket No. 6690-UR-116 (December 21, 2004.) WPSC requests that the Commission again set its common equity range on a financial basis of 54% to 58%. (Tr. 278.) The Commission should reject this request because business



risk is not as great for WPSC as it asserts and because the higher equity levels cost ratepayers millions of dollars but fail to provide adequate offsetting ratepayer benefits.

In support of its request, the Company through one of its witnesses asserts that “[b]usiness risk is greater today than in earlier years.” (*Id.*) In his testimony identifying risks facing the utility industry, Mr. Bradley Johnson (Vice-President-Treasurer of WPSR and WPSC) identified a number of possible concerns that read like a boilerplate list used repeatedly in rate proceedings over the years. On cross-examination by CUB, however, Mr. Johnson acknowledged that several of the risk factors he identified were simply not applicable to WPSC for the test year, including the threat of retail access, ISO formation and nuclear ownership. (Tr. 271; 275-76; 343-45.)

Moreover, there appears to be little ratepayer benefit of a higher equity range. As noted by Staff, the current 54% to 58% range set by this Commission for WPSC has not prevented the utility’s ratings from sliding, and WPSC now carries a corporate rating of “A+”. (Tr. 458.) WPSC’s rating is undoubtedly tied to the rating of its parent holding company, WPS Resources (“WPSR”). WPSR’s corporate rating is “A” and WPSC is unlikely to get upgraded unless WPSR’s rating improves. (*Id.*) Importantly, 108 of 110 Integrated Electric, Gas and Combination Utilities have ratings lower than WPSC’s “A+” rating, making it questionable why this Commission would feel obliged to raise WPSC’s rating still further. (*Id.*)

The cost of higher equity levels cannot be ignored. At CUB’s request, Staff prepared Delayed Exhibit 38 which details the difference between 54.24% and 52% common equity on a financial basis in terms of ratepayer impacts. The slightly lower equity level of 52% results in ratepayer savings of \$5.1 million if the Company replaces equity with short-term debt, \$4.6 million if the Company replaces equity with long-term debt.

Because of the questionable benefit and definite higher costs to ratepayers of supporting the higher equity ranges favored by WPSC, CUB requests that the Commission establish a long-term equity range on a financial basis no higher than 45% to 52.1%, the range necessary for the Company to support an A rating. (*Id.*)

**IV. THE COMMISSION SHOULD SUPPORT CONTINUED PROGRESS FOR IMPROVED RATE DESIGN OPTIONS AND SMALL CUSTOMER LOAD MANAGEMENT INITIATIVES.**

Faced with higher rate increases, customers need more rate design options that result in savings not only for themselves but that offer savings to the utility itself. As part of this rate proceeding, the Commission can move WPSC closer to developing those rate designs, just as it has moved the Company closer to developing small customer load management programs.

**A. The Commission Should Renew Its Support Of WPSC Developing Small Customer Load Management Options In Collaboration With CUB And Should Order WPSC To Further Implement Innovative Rate Designs In Conjunction With This Effort.**

In WPSC's last rate case in Docket No. 6690-UR-116, the Commission ordered the Company to work with CUB to develop small customer load management options. (Tr. 113-14.) Since that last rate case, CUB and WPSC have, in fact, been meeting and making progress as noted by PSC Staff:

This summer WPSC is conducting several load management pilots. WPSC's current HELP program controls appliances using an FM-based signal. In one of its pilots, WPSC is testing the use of a different technology that uses an adaptive cycling algorithm. Several control strategies will be tested with the cycling algorithm technology. In another pilot, WPSC is testing use of programmable thermostats to control appliances. As with the HELP pilot, several control strategies will be tested. Additionally, WPSC and CUB have reached an agreement to explore opportunities for multi-market providers to deliver small customer load management options. . . . The Load Management Collaborative has resulted in significant progress in exploring and testing load management opportunities for small customers. These are important first steps in the development of new options.

(Tr. 114.)

CUB recognizes that the Company has done a commendable job in the collaborative process, but submits further work and evaluation must be done on the pilot programs and rate design alternatives. (Tr. 869.) To this end, the Commission should state that it finds value in the efforts of the collaborative, and that it requires the Company jointly with CUB to file a report in March 2006 concerning the results of the pilot programs, further options to be developed—for both load management and rate design—and a timeline for such efforts. (Tr. 888.) Continued reporting requirements and oversight by the Commission can help ensure that ratepayers receive the benefit of small customer load management programs on an appropriate time frame.

In response to CUB testimony in this proceeding concerning the development of rate designs that afford small use customers greater usage options, WPSC suggested that those efforts were already being developed in conjunction with the small customer load management collaborative. (Tr. 798.) CUB will in good faith work with WPSC towards this end. CUB believes that WPSC should offer small customers a menu of time-of-use rate options that will optimize customer participation. (Tr. 863-64.) One size does not fit all. The collaborative should explore this menu approach further.

**B. CUB Supports Equalizing Customer Charges For Small Customers Whether On Time-Of-Use Or Flat Rates.**

One action the Commission can take now to remove barriers to small customer alternative rate designs is to adopt Staff's proposal to equalize customer charges for small customers whether on TOU or flat rates. (Tr. 680-81.) The new automatic meter reading devices in place for WPSC's small use customers permit TOU readings without installing a different meter. (Tr. 680.) Commission adoption of uniform customer charges may remove a barrier to participation in the program. (Tr. 680-81.)

WPSC supports uniform customer charges but would instead raise the customer charge for non-TOU customers until those charges reach TOU customer charge levels. (Tr. 796-97.) PSC Staff has proposed to recoup WPSC's lost revenues caused by a smaller TOU customer charge by increasing energy charges for small customers. (Tr. 680-81.) CUB agrees with Staff's approach of raising energy charges because such a move sends the right signal to customers concerning the price of energy and, in effect, heightens the reward for accomplishing energy savings. (Tr. 887.)

**V. COSS STUDIES IN THIS PROCEEDING SUPPORT A LOWER INCREASE FOR SMALL USE CUSTOMERS THAN PROPOSED BY THE COMPANY AND STAFF, AND SHOULD BE FOLLOWED TO AVOID HARSH RESULTS FOR RESIDENTIAL CUSTOMERS.**

Staff has proposed that the small use customer class receive a 5.5% increase, commercial customers a 7.3% increase and industrial customers an 8.7% increase as compared to a 6.7% company-wide revenue hike at the staff-audited revenue requirement. (Ex. 45, Schedule 1, Page 1.) In contrast, using the same revenue requirement, WPSC proposed that the small use customer class receive a 7.7% increase, commercial customers a 7.9% increase and industrial customers a 3.4% increase. (*Id.*) Revenue allocation that follows appropriate COSS suggests that even Staff's proposal places an undue burden on the small use customer class. Moreover, using a comparison of percentage revenue allocation to the percentage company-wide revenue increase distorts the impacts of actual dollar and cent impacts to ratepayers. Once per kWh average charges are taken into account, it becomes apparent that small use customers are being asked to pay a disproportionate share of WPSC's costs.

**A. The Staff TOD and Location COSS Provide An Appropriate Range For This Commission To Consider In Establishing Class Revenue Allocations.**

Staff submitted different types of COSS, including a Location COSS which allocates production costs on both energy and demand, allocates energy both for on-peak and off-peak cost, appropriately allocates costs associated with the KNPP PPA and does not use a minimum distribution system to allocate distribution costs. (Exh. 45, Schedule 2, Page 2 of 2, Table 3.) This COSS shows that small use customers should actually receive a decline in revenue allocation of -.21%. Staff's TOD COSS, which does include a minimum distribution system approach, combined with the Location COSS, provide an appropriate range of COSS results. The TOD COSS suggests that an increase of 4.21% for small use customers is warranted although, as explained below, this result is extreme due to the use of a minimum distribution system approach. (Tr. 873.)

Allocating production costs on both demand and energy is consistent with principles of cost-causation, and CUB endorses the use of Staff's equivalent peaker method in the Location and TOD COSS towards this end. (Tr. 672-73, 837-38, 879-82.) The equivalent peaker method recognizes that baseload plants, for instance, are built to provide more inexpensive energy as well as to meet demand. The equivalent peaker method is hardly a radical approach to COSS. In their pending rate cases, both Xcel and WEPCO have followed COSS methodologies that allocate production costs on demand and energy. Xcel allocates 44% on demand and 56% on energy; WEPCO allocates 62% on demand and 38% on energy. (Tr. 718.)

The Staff TOD and Location studies also correct for WPSC's failure to include interruptible demand from firm coincident peak allocators. (Tr. 674.) This failure permits interruptible customers to avoid paying for costs created by their usage. (*Id.*) As CUB witnesses

Edgar and De Forest stated, there is no basis for excluding interruptible customers from paying for a portion of the fixed production costs related to baseload plants. (Tr. 884-85.) Including interruptible load in the demand allocator but providing an interruptible credit based on the cost of a peaker, as Staff has done, is a better approach. (Tr. 885.)

CUB prefers the Location COSS over the TOD Study because the former does not use the minimum distribution system (“MDS”) method to allocate distribution costs. MDS requires the cost analyst to posit a fictional barebones distribution system and to allocate those costs to customers with the remaining distribution system assigned to demand. CUB has stated in numerous rate cases its reasons for its opposition to MDS and it will not repeat those arguments here.<sup>4</sup>

Additionally, the Staff TOD and Location COSS shown in Ex. 45 in Table 3 properly allocate the costs associated with the Company’s PPA with Dominion Energy Kewaunee. Insisting on elevating form over substance, WPSC proposes to allocate the KNPP PPA’s fixed and variable charges as demand and energy. (Tr. 32.) CUB opposes this allocation for two reasons. First, in the specific instance of the KNPP PPA, WPSC has testified that it was established to approximate the cost to WPSC and WPL of continuing to own the KNPP. (Tr. 676-77.) It is therefore appropriate to allocate the costs of the PPA as if KNPP were still owned by WPSC and WPL. Second, CUB submits that PPAs should be analyzed on the basis of cost causation. CUB believes that the general rule for allocating PPA capacity costs is that capacity costs incurred to ensure reliability should be allocated on an appropriate demand allocator while capacity costs that are incurred to acquire energy at a lower cost than otherwise

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<sup>4</sup> Messrs. Edgar and De Forest offered a detailed critique of MDS in their prefiled testimony. (Tr. 845-852.)

available should be allocated as “capitalized energy” costs on the basis of on/off peak energy usage. (Tr. 871.)<sup>5</sup>

CUB proposed a cost of service result that continued the use of a “minimum distribution system” approach included in the Staff TOD study but limited in the second step the most extreme allocation impacts of MDS and A&G costs to reflect the lack of strong justification for the treatment of what are essentially unallocable costs.<sup>6</sup> Under this approach, the COSS result would be lower than the Staff TOD study – in the range of a 0.17 cents per kWh increase for residential customers as indicated in Exh. 56, Sch. 1.

WPSC asserted that CUB’s suggested “2-step approach” to revenue allocation not be used until first addressed in the Commission’s generic COSS proceeding in Docket 05-EI-137. (Tr. 40.) No persuasive reason exists, however, for the Commission not to use this approach in this proceeding. The allocation of costs includes some costs that can be directly assignable on cost causation and many others that must be indirectly assigned. (Tr. 884.) The 2-step approach allows the Commission both to understand the range of impacts from how these latter costs are allocated as well as to moderate inappropriate impacts (e.g. from an MDS approach if used or for unallocable A&G costs). (See Exh. 56.) It allows the Commission to consider the impact of such allocations rather than to have to choose with little guidance within a wide range of COSS results. The 2-step approach provides a useful basis for the Commission to consider where within a range of COSS, the ultimate decision on what is allocated to the various classes should be for individual as well as aggregate costs, especially for costs that are not strongly related even in an indirect manner to cost causation.

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<sup>5</sup> WPSC also testifies that if the fixed costs of the KNPP PPA are allocated on the basis of energy, the return of NQF monies should be allocated in the same manner. No reason exists to follow such an approach. If WPSC raised these NQF monies as a cost allocated on demand, then those monies should be returned in the same manner. (Tr. 886.)

<sup>6</sup> Allocations to large industrial customers were not affected by step 2.

**B. The Use Of The Average Percentage Rate Increase As A Benchmark To Determine The Fairness Of Revenue Allocations Creates Misleading Results And Can Lead To Decisions That Move Rates Away From COSS Results.**

CUB acknowledges that Staff has proposed that residential customers receive a lower percentage rate increase than the average percentage rate increase. But use of this benchmark—the average percentage rate increase—to determine the fairness of proposed rate increases by customer class can have misleading results. CUB submits that such an outcome is present here. Staff's proposed lower than average percentage rate increase for residential customers actually moves *away from*, rather than toward, the results shown in the TOD COSS when seen in terms of cost per kWh. The following chart demonstrates CUB's concern:

	Staff Increase (cents/kWh)	% Above Average per kWh Increase	TOD as % of Staff Increase	TOD Increase (cents/kWh)
<b>Average</b>	<b>0.47</b>			
<b>Residential</b>	<b>0.58</b>	<b>23%</b>	<b>76%</b>	<b>0.44</b>
<b>Commercial</b>	<b>0.46</b>	<b>-2%</b>	<b>63%</b>	<b>0.29</b>
<b>FG-2 &lt; 50kW to Cg-2</b>	<b>0.50</b>	<b>6%</b>	<b>82%</b>	<b>0.41</b>
<b>Fg-4 to Cg-4</b>	<b>0.50</b>	<b>6%</b>	<b>82%</b>	<b>0.41</b>
<b>CP-1 Industrial</b>	<b>0.38</b>	<b>19%</b>	<b>158%</b>	<b>0.60</b>

(Tr. 874.) While Staff's TOD COSS indicates that residential rates should receive only a 0.44 cent per kWh hour increase, Staff's proposal results in a 0.58 cent per kWh hour increase above the average per kWh increase of 0.47 cents. *Significantly, then, a lower than average percentage rate increase translates into an above average increase in kWh charges.* The result is that the residential class will in fact bear a disproportionate amount of the proposed rate increase in this case despite the results of the COSS. This result also exacerbates any effort to move toward cost of service in future cases. (*Id.*) CUB believes that the more appropriate COSS



results are shown in its “moderated” Staff TOD study which indicated that the residential class should receive no more than a 0.17 cents per kWh increase. (Exh. 56, Sch. 1.) However, if the Commission determines that there are non-COSS reasons to moderate the increases for other classes, small customers should receive no more than the average per kWh rate to at least not exacerbate current COSS relationships. (*Id.*)

**C. Staff’s Revenue Allocation Effectively Shifts The Costs Of Variable Interruptible Credits For Industrial Customers Onto Other Customer Classes.**

Staff has proposed to moderate the percentage rate increase for industrial customers to no more than 2% of the overall change in revenue authorized by the Commission to offset the impacts of WPSC replacing its fixed interruptible credit for industrial customers with a variable credit. (Tr. 685.) If the PSC disapproves the adoption of a variable interruptible credit, Staff recommends “the Commission may wish to set a higher limit for the increase of the CP class in order to better reflect COSS analysis results.” (*Id.*)

Staff’s 2% limit on industrial customers effectively shifts the recovery of more costs to other customer classes in order to protect certain CP-1 customers (i.e. lower load factor) from the proposed credit change combined with the general class revenue increase in this case. It does so by limiting the overall cost increase to be recovered from the CP-1 class in spite of COSS results that show a higher overall increase is appropriate and warranted. In effect, Staff has taken an intra-class shift in costs and lowered the overall increase to the CP-1 class. The result of this shift is that other customer classes must pay even more than what appropriate COSS indicate. (Tr. 871-73.) WPSC has not demonstrated a compelling need to adopt the variable credit option as abruptly as it has proposed. (*Id.*) In their testimony, CUB witnesses Edgar and De Forest proposed a transition method of moving towards a variable credit by decreasing the immediate

reduction of the existing fixed credit and not raising the existing variable credit as much as proposed. (Tr. 872-73.) Transitioning to the use of variable credits would provide the Commission with an option short of rejecting variable credits altogether and would also help mitigate the inappropriate shifting of costs to other customer classes resulting from Staff's proposed 2% above-the-average percentage rate increase for the industrial class. (*Id.*)

**D. Asking Residential Customers To Pay More Than Appropriate COSS Results Indicate Is Harsh, Especially When Facing Dramatically Higher Rates.**

CUB understands that the Commission may take other factors into account besides COSS results when it determines revenue allocation by customer class. But asking residential customers to pay more than what appropriate COSS results show is a harsh result in the face of dramatically rising energy prices. As CUB witness George Edgar noted, real median household income in Wisconsin has fallen by more than \$4,000 since 1999. (Tr. 875.) Real median wages are only about 5% (68 cents) higher than 25 years ago. (*Id.*) Poverty in Wisconsin has increased by almost two percentage points in the last few years. (*Id.*) Increases in costs for necessities such as gasoline and health care among others have severely pinched the available incomes of these many persons in Wisconsin whose economic situation has not substantially improved. (*Id.*)

The effects of rate increases to the residential customer class are not limited to just that class, however. The results can well be decreased ability to purchase local products and services, and/or increased governmental expenditures. Therefore, shifting costs that a range of appropriate COSS indicate should be borne by others to the residential class will and should be expected to have undesirable impacts that can harm improved economic growth in Wisconsin, as well as the quality of life for many of its citizens. (Tr. 875-76.) Each of these problems is compounded by inappropriate allocations in the face of dramatically increasing electric and gas rates.

**E. The Increased Natural Gas Costs Of WPSC For Electric Generation Should Be Allocated On Energy.**

At hearing, Staff asked each COSS expert witness for his views concerning how to allocate the projected higher energy costs resulting from the \$58 million boost in natural gas rates above the prices Staff had assumed in its audit of WPSC's rate filing. There was wide consensus among CUB, WIEG and Wausau Paper Corporation witnesses that these costs should be allocated on the basis of on- and off-peak energy with WIEG appropriately expressing concern that the focus of cost allocation should be on the utility's entire costs and not just on one additional amount. (Tr. 637-639, 890, 909.) Staff witness Dr. Petersen stated that while he would normally follow this approach, he believed resulting rate impacts might not be acceptable to the Commission. (Tr. 697-98.)

CUB believes that COSS should follow cost-causation principles. If necessary and deemed desirable, revenue allocation and rate design are the places to mitigate COSS results. A COSS should accurately reflect costs, nothing more and nothing less. CUB submits that the best way to address natural gas costs is to reduce to the maximum extent possible WPSC's revenue requirement in the first instance.

**VI. CONCLUSION.**

For the reasons stated above, the Commission should: 1) reject WPSC's KNPP Wind-Up Plan; 2) adopt ROE and capital structure decisions that help mitigate dramatically rising rates; 3) continue its support of the CUB-WPSC collaborative on load management and rate design; and 4) adopt customer class revenue allocations that more closely follow COSS results that best follow cost-causation principles.

Dated this 28<sup>th</sup> day of October, 2005.

Respectfully submitted,

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